

Credit FAQ:

Potential Scenarios Of Braskem S.A.'s Sale

May 23, 2023

This report does not constitute a rating action.

On May 9, 2023, Braskem S.A. (BBB-/Stable/--) disclosed details about a non-binding offer that its shareholder, Novonor S.A., received from Apollo Management X, L.P. and ADNOC International Limited - Sole Proprietorship L.L.C. for its 38.3% stake in Brazilian petrochemical company. Novonor has the intention to sell its stake in Braskem for several years. Novonor is evaluating the offer and hasn't made a decision to accept it. Here, S&P Global Ratings responds to the frequently asked questions from investors about the potential rating impact on Braskem stemming from a change in its shareholders' structure, as well as our expectations of the company's future performance.

Frequently Asked Questions

Does the current ownership of Braskem have any rating impact?

We currently assess Braskem as insulated and delinked from the credit quality of its shareholders Novonor (not rated) and Petróleo Brasileiro S.A. – Petrobras (BB-/Stable/--), because we view Braskem's financial performance as independent and separate from both entities, given the existing shareholders' agreement that's in place until 2045. Novonor controls 38.3% of Braskem's total shares and 50.1% of voting shares, while Petrobras holds 36.1% and 47%, respectively. According to the shareholders' agreement, all decisions between Novonor and Petrobras should be taken in a consensual way, which limits Novonor's ability to exert full control over Braskem's cash flows.

What are the potential rating scenarios after Novonor accepts a binding offer?

If Novonor sells its stake to a new shareholder and Petrobras retains its current stake.

Regardless of the credit quality of the new shareholder(s), we would likely keep our view of Braskem as insulated and delinked, because neither Petrobras nor the new shareholder would be able to exercise control on its own. A new entity acquiring only Novonor's stake would adhere to the existing shareholders' agreement, and assume all the rights, benefits, liabilities, and obligations as those of Novonor's, according to Clause 7.9 of the shareholders' agreement.

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If Petrobras decides to exercise its right of first refusal and buy Novonor's stake under same conditions offered by a third party. This would most likely trigger a downgrade of Braskem to the level of Petrobras ('BB-'). This is because Petrobras would hold 97% or more of Braskem's voting rights. According to our methodology, the rating on a subsidiary is in most cases limited to that of its ultimate parent, because the latter can define and influence the subsidiary's strategic decisions related to leverage, investments, shareholder remuneration, etc. The rating cap is generally the case, unless there are factors that could allow an entity to be insulated from its parent. Given the current ratings on Braskem and Petrobras, to avoid a downgrade of Braskem, we would need to see several insulation conditions, including an existence of significant minority shareholders with an active economic interest, along with regulatory protections or restrictions that would prevent Petrobras from impairing Braskem's creditworthiness, among other aspects.

If Petrobras decides to exercise its tag along (which we believe is the most unlikely scenario at this point), resulting in a single controlling shareholder, which is a financial sponsor. This could lead to Braskem's downgrade. We define a financial sponsor as an entity that follows an aggressive financial strategy in using debt to maximize shareholder returns. Accordingly, the financial risk profile we assign to companies that are controlled by financial sponsors ordinarily reflects our presumption of some weakening in credit quality in the medium term. Specifically, at the current rating on Braskem, to avoid a downgrade in this scenario, we would need to see other shareholders owning a large stake (generally at least 20%), along with the sponsor relinquishing control over the intermediate term, Braskem's leverage to remain in line with current levels (3x-4x) or below, and for its liquidity to remain at least adequate. However, if there is a mix of financial sponsor and strategic shareholder, as indicated in the non-binding offer, we would need to understand the new shareholders' structure, board composition, decision-making process, as well as potential changes in Braskem's strategy and financial policy to assess if these factors could change our view of Braskem's current credit quality.

What are the covenants related to change of control in the company's bonds?

All of Braskem's bonds have a payment-acceleration clause if the issue ratings on them are lowered as a result of a change of control. In general, these clauses mention a period of 90 days after the change of control occurs. We would need to monitor the acceleration risk in case a change of control prompts a negative rating action on the company.

What is your view of current industry conditions and potential impact on Braskem's leverage and ratings?

Since mid-2022, the petrochemical industry has been facing limited demand growth, given concerns over the potential recession or low growth in the U.S. and Europe and uncertainties about China's recovery, combined with high feedstock costs and new capacity coming online, reducing spreads sharply. After Braskem's weak fourth-quarter results, its first-quarter results showed some signs of recovery in terms of profitability, but the industry prospects will remain challenging for the next few quarters. We currently forecast the company's debt to EBITDA at about 4.0x for 2023 but declining to about 3.0x in 2024. Braskem's management has already begun countercyclical measures such as cost reductions, capex cuts, and improvements in working capital. Also, management is committed to keep the investment-grade rating. We still have a stable outlook on our rating on Braskem because we believe that it will navigate this cycle and maintain leverage at 3.5x or below on a three-year moving average.

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